NO. 84824-6

IN THE SUPREME COURT
OF THE STATE OF WASHINGTON

CITY OF TACOMA, a municipal corporation,

Appellant,

v.

CITY OF BONNEY LAKE, CITY OF FIRCREST, CITY OF UNIVERSITY PLACE, CITY OF FEDERAL WAY, PIERCE COUNTY and KING COUNTY,

Respondents.

BRIEF OF RESPONDENTS CITY OF FIRCREST, CITY OF UNIVERSITY PLACE, CITY OF FEDERAL WAY, AND PIERCE COUNTY

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I. INTRODUCTION

This is a case about contract rights—specifically, the right of a party to rely upon a long-standing agreement to provide a service and to defend, indemnify, and hold it harmless. Respondents City of Federal Way, City of Fircrest, City of University Place, and Pierce County have franchises with the City of Tacoma that make Tacoma responsible for maintaining all the components of its water system located within their jurisdictions. In seeking to enforce the contract rights within these franchises, the Respondents do not intend to dodge the implications of this Court's holding in *Lane v. City of Seattle*, 164 Wn.2d 875, 194 P.3d 977 (2008). Rather, the Respondents' position is fully consistent with *Lane*.

Until late 2008, when Tacoma decided to bill the Respondents for fire hydrant services, Tacoma Public Utilities (TPU) provided this service without requiring the payment of money. The franchises extended a valuable benefit to TPU in exchange—a guarantee that as long as the franchises remain in effect, TPU can expand, maintain, and repair its infrastructure within Respondents' jurisdictions. In the franchise agreements, TPU also promised to hold each jurisdiction harmless from "any and all costs" arising by virtue of TPU's presence in each jurisdiction.

Tacoma erroneously asserts that *Lane* made it illegal for TPU to provide fire hydrant services, unless the Respondents pay in cash. But *Lane* does not prohibit TPU from providing services to the Respondents under a mutually-beneficial franchise. Tacoma also erroneously asserts that the hold harmless provisions of the franchises only protect the Respondents from classic third party tort claims. But these provisions are worded broadly enough to prohibit Tacoma from compelling the Respondents to pay for fire hydrants or pursuing this action against them.

Finally, Tacoma erroneously asserts that enforcing the franchises as written, and as understood by the parties for a decade or more, would violate public policy. According to Tacoma, if the Respondents do not pay for fire hydrants, Tacoma ratepayers ultimately will be forced to bear that cost, in contravention of *Lane*. This argument has three fatal flaws. First, the issue of how Tacoma chooses to finance fire hydrant costs, in the event that it cannot recover such costs from the Respondents, is not before the Court. Second, if Tacoma did elect to increase rates to account for costs attributable to extra-territorial fire hydrants, this would not violate *Lane*, because *Lane* allows a utility to recoup its business costs through rates. Finally, *Lane* does not preclude the parties from negotiating broad hold

harmless provisions that shield the franchisors from all costs associated with the franchises.

Regardless of how this Court rules on the threshold issues of whether the Respondents must pay for fire hydrants, it cannot resolve the question of how much must be paid. The Respondents have never conceded that Tacoma's cost calculations are correct. Moreover, due in part to Tacoma's failure to answer the Respondents' discovery requests prior to moving for summary judgment, there is almost no evidence in the record explaining Tacoma's cost calculation methodologies. This Court should decline to make any ruling regarding the propriety of Tacoma's calculations, or which components of the water system can be included in those costs.

As support for the argument that the Respondents "must" pay for the general government expense of fire hydrants, Tacoma relies solely upon broad language in *Lane* that did not address the precise questions before this Court: whether a franchise can obligate a franchisee to continue providing a service in exchange for the valuable benefits it receives, and whether broad hold harmless provisions preclude the franchisee from suing the franchisors. Because the law firmly supports affirmative answers to

these questions, the trial court's order of summary judgment must be sustained.

II. COUNTER STATEMENT OF THE CASE

A. Tacoma's water system and its presence in Respondents' jurisdictions

The City of Tacoma has an enormous water system operated by Tacoma Public Utilities (TPU), which occupies much of Pierce County and sprawls into King County. CP 184. Though TPU is headquartered in Tacoma, it has ratepayers throughout Pierce and King Counties, expanding TPU's ratepayer base far beyond Tacoma's taxpayer base. *Id.* TPU's water mains run underneath the streets and other properties of neighboring jurisdictions. CP 184-85. Some of these jurisdictions have franchise agreements with TPU, and some of them do not. *Id.*

Regardless of where their water comes from, local governments like the Respondents must enforce the fire flow mandates of the International Fire Code, which the State requires all cities and counties to adopt. RCW 19.27.031. Fire hydrants themselves are but one increment of fire suppression services. CP 498 ("[H]ydrant system would be worthless if it did not have sufficient water pressure and water storage necessary to operate the hydrants."). Fire suppression also requires that fire hydrants be connected to water mains that supply adequate fire flow. CP 619-20.

Tacoma calls the costs attributable to fire suppression "Public Fire Protection (PFP)" expenses. CP 623. Using a formula, Tacoma came up with a charge of $303.10 per year for each fire hydrant. *Id.*[1] Tacoma then sent bills to the Respondents, requesting payment of large sums the Respondents had neither anticipated nor budgeted for. *See, e.g.*, CP 85, 620.

B. Tacoma's franchises with the Respondents.

1. The franchises make Tacoma solely responsible for its water system, including "appurtenances" used for fire suppression.

TPU signed franchise agreements with the Respondents, thereby establishing a contractual relationship with each. CP 190-200 (Fircrest franchise); 202-222 (University Place franchise); CP 224-243 (Federal Way franchise); CP 250-276 (Pierce County franchise). The franchises give Tacoma the right to "construct, operate, maintain, replace, and use all necessary equipment and facilities for a water system" within the franchise area. *See, e.g.*, CP 191. Water facilities are defined to include water pipes, mains, appurtenances, and accessories "necessary for the transmission and

[1] The Respondents do not concede or agree that Tacoma's method of calculating the costs of fire suppression services is appropriate or correct. The trial court did not reach this issue below, and an insufficient record exists. The Respondents dispute, among other matters, whether the oversizing of water mains is properly included in costs, when this is an expense TPU, for the most part, did not bear. CP 626-27; *infra* Part III.G of this Brief.

distribution of water." *See, e.g.*, CP 225. None of the four franchises requires the Respondents to pay cash for fire hydrant services.

Tacoma's assertion that the franchises "fail to mention fire hydrants, fail to detail the intent of the parties regarding fire hydrants, and fail to state what consideration was paid for providing fire hydrants" (Brief at 5) is disingenuous. There could be no dispute that the franchises concern TPU's water system, of which fire suppression is a part.[2] Tacoma has acknowledged that the hydrants themselves, along with the additional storage and delivery capacity linked with them, benefits that water system by facilitating maintenance. CP 86 ("Tacoma water uses hydrants and the associated additional storage and delivery capacity for system maintenance purposes, which is of benefit to our ratepayers."). TPU even deducts from its PFP calculations a percentage it believes is attributable to use of the fire suppression system for maintenance. *Id.*

2. The franchises require Tacoma to hold the Respondents harmless from "any and all" costs arising from the franchises.

The four franchise agreements all contain broad provisions that require Tacoma to defend, indemnify, and hold each Respondent harmless

[2] Federal Way's franchise explicitly mentions fire hydrants. It requires TPU to notify the fire district if "it is necessary to shut down or diminish water pressure so that fire hydrants may be affected." This statement is an acknowledgement by TPU that hydrants are inseparably linked to the water system. CP 230.

from any claim or cost arising from the franchises. CP 195, Fircrest Franchise ("The Grantee hereby releases, covenants not to bring suit, and agrees to indemnify, defend, and hold harmless the City . . . from any and all claims, costs . . . to any person . . . , including claims arising . . . by virtue of Grantee's exercise of the rights granted herein."); CP 212, University Place Franchise ("Grantee hereby releases, covenants not to bring suit and agrees to indemnify, defend and hold harmless the City . . . from all claims arising against [University Place] by virtue of [University Place's] ownership or control of the rights-of-way or other public properties by virtue of [TPU's] exercise of the rights granted herein."); CP 235, Federal Way Franchise ("Franchisee agrees to indemnify and hold harmless and defend the City . . . from any and all claims, demands, losses, actions and liabilities . . . resulting from or connected with this Franchise . . ."); CP 253, Pierce County Franchise ("Grantee . . . agrees to defend, indemnify, and save harmless Pierce County . . . from and against all liability, loss, cost, damage, and expenses . . . arising . . . out of or in consequence of the construction, installation, operation or maintenance of any equipment or facilities, inclusive of appurtenances thereto, under the franchise.").

3. Tacoma was not forced into the franchises.

Tacoma suggests that it was forced to sign franchise agreements with the Respondents (Brief at 7), but nothing in the record supports this contention. The franchises recite the valuable benefits TPU receives, including certainty that its infrastructure can remain, and confidence in its ability to plan. CP 192, 207 ("The consideration for this agreement includes, but is not limited to, the mutual and individual benefits of this agreement that allow each of the parties the ability to make long term planning decisions in light of the provisions set forth herein."). The franchises also afford TPU a measure of certainty that it can keep its enormous rate base intact, rather than seeing its territory eroded by rival water systems. CP 667. Perhaps because it recognizes the benefits it receives, TPU has never requested that any of the franchises be terminated. In fact, in June 2009, six months after the *Lane* decision was issued, TPU agreed to extend Federal Way's franchise. CP 551.

Federal Way and Pierce County do not charge Tacoma any franchise fee at all. CP 238, 250-276. Fircrest and University Place do charge a fee. However, their franchises, unlike the other two, obligate them not to "compete" with TPU. CP 216-17, 196.

C. Taxpayer costs vs. ratepayer costs—*Okeson v. City of Seattle.*

In 2003, the Washington State Supreme Court decided *Okeson v. City of Seattle*, 150 Wn.2d 540, 78 P.3d 1279 (2003), the case that set the instant dispute in motion. In *Okeson*, the Court precluded Seattle City Light (SCL) from adding to its electric bills a charge to pay for street lights city-wide. *Id.* at 554. Street lights serve the general government function of lighting the path of travel, rather than a specific utility function of selling a commodity to a customer. *Id.* at 550. Therefore, the charge on ratepayer bills constituted a "tax" rather than a "fee." *Id.* at 554. Taxes, unlike fees, must be imposed only after following state constitutional provisions on enactment of taxes. *Id.* at 556. Specifically, a city must have statutory authority to enact the tax, indicate that the charge is a "tax," adopt it using proper procedures, and expressly state that the tax is subject to referendum. *Lane*, 164 Wn.2d at 886.

Recognizing the similarities between fire hydrants and street lights, after *Okeson* Seattle Public Utilities (SPU) removed the cost of fire suppression services from water rates, and Seattle began paying these costs out of its general fund. *Lane*, 164 Wn.2d at 880. Seattle raised revenue to cover the expense by increasing the utility tax on SPU. *Id.* SPU, in turn,

raised rates to cover the utility tax. *Id.* Thus, the end result was that ratepayers were still paying for fire hydrants, albeit indirectly.

D. Offspring of *Okeson—Lane v. City of Seattle.*

Okeson spawned a number of "tax vs. fee" disputes, including *Lane v. City of Seattle.* In *Lane*, the plaintiffs argued that because fire hydrants are fundamentally a general government service "for which the general government must pay," SPU could not recoup the utility tax it paid to Seattle via an increase in rates. *Lane*, 164 Wn.2d at 886. ("Lane complains that Seattle is frustrating the holding in *Okeson.* He argues that raising taxes on SPU and passing the increases along to ratepayers is just the same as SPU charging ratepayers for hydrants.").

The Supreme Court dismissed this challenge out of hand, finding that the *Okeson* mandate was satisfied when Seattle enacted the utility tax pursuant to the constitution. *Id.* at 886-87 ("The law is not that Seattle must charge for hydrants to a broad range of taxpayers. Instead, it is simply that cities must have statutory authority to impose taxes and must enact them properly as 'taxes.'"). In other words, *Lane* does not mandate that taxpayers, as opposed to ratepayers, must ultimately bear the costs of fire hydrants. *Id.* Implicit in *Lane* is the recognition that a utility can recoup its business expenses—in that case, the utility tax increase on SPU—via rates,

even if the end result is that ratepayers indirectly bear the cost of a general government service.

The *Lane* Court also ruled that the City of Lake Forest Park had to compensate Seattle for the cost of fire hydrants located within its city limits. *Id.* 889-90. Lake Forest Park lacked a franchise with SPU. The *Lane* trial court had dismissed from the lawsuit other jurisdictions with whom SPU did have franchises, including the City of Shoreline and King County. CP 420-21.

Judge Michael Spearman gave two reasons for dismissing Shoreline and King County. First, the language of the franchise agreements indicated that SPU would be solely responsible for "equipment, lines and appurtenances which are used in the operation, maintenance, repair or construction of the grantee's service and which are located within the county road rights-of-way." CP 420. Judge Spearman ruled that this language demonstrated SPU's intent to cover the costs of operating a water system within the franchise area; thus, Seattle waived any claims for reimbursement for fire hydrant services when it executed the franchises. *Id.*

Second, Judge Spearman cited the broad indemnity provisions of the franchises, stating:

> [B]oth King County's and Shoreline's franchise agreements include indemnification clauses [which] provide that SPU shall hold Shoreline and King County harmless from claims arising from exercising the rights granted under the franchise agreement. . . . Thus, even though Shoreline and King County may have otherwise been liable on Seattle's third party claims, the Court finds that such liability is precluded by the agreements both parties have entered into.

CP 420-21.[3] Seattle did not appeal the dismissal of King County or Shoreline.

E. **Franchises alter the "tax vs. fee" debate—*Burns v. City of Seattle.***

In 2007, the Supreme Court decided *Burns v. City of Seattle*, 161 Wn.2d 129, 164 P.3d 475 (2007), its seminal case on how franchises affect the "tax vs. fee" debate. The *Burns* plaintiffs alleged that SCL's franchise agreements with neighboring cities, which required SCL to pay a percentage of revenues to these cities, violated the state law prohibiting franchise fees on electrical utilities. *Id.* at 134-35. This Court rejected that argument, finding that the fees were specifically negotiated in exchange for promises not to start rival electrical utilities that would undercut SCL's market share and rate base. *Id.* at 150-51 ("The payments at issue in this case are not

[3] Judge Spearman used the term "third party claim" because in *Lane*, Seattle sued Shoreline and King County as third party defendants. Shoreline and King County, though third party defendants in *Lane*, are similarly situated to the Respondents in this case because TPU (the franchisee) has brought a claim against them (the franchisors), just as Seattle did in *Lane*.

governmental charges but, like water rates, are proprietary charges voluntarily incurred in the context of a proprietary transaction.").

The *Burns* Court emphasized the value a franchise conveys to a utility, in the form of certainty that it can keep its infrastructure, and rate base, intact. *Id.* at 156 ("Presumably, such a voluntary exchange will enhance, not impair, a utility's ability to provide cost-effective service to its customers . . . ."). The *Burns* Court also reiterated that a utility's decision to enter into a franchise is entitled to deference from the courts, because franchises are exercises of proprietary authority. *Id.* at 155. For all these reasons, the Court declined to interfere in the contractual relationship between the franchisee and franchisors.

F. Tacoma sues its franchisors, the Respondents.

Prior to *Lane*, Tacoma had not been severing the estimated costs of fire hydrants from the costs of operating a water system; rate payers footed the whole bill. CP 186. The cost of fire hydrants was therefore spread out over TPU's ratepayer base, which is broader than Tacoma's taxpayer base because TPU reaches beyond Tacoma. After *Lane*, TPU removed from its rates what it believed to be the cost of providing fire hydrant services, and started paying from its general fund the costs of hydrants within the Tacoma city limits. *Id.* TPU sent bills to all the Respondents, seeking to

collect for hydrants located in their jurisdictions, including the connections to, the oversizing of, and the operation and maintenance of, the water mains.[4] *See, e.g.*, CP 619-20. The Respondents refused to pay, citing their franchises. On June 12, 2009, Tacoma filed the instant lawsuit.[5]

G. The Respondents are granted summary judgment.

In April 2010, the Respondents moved for summary judgment, arguing that the franchises obligate Tacoma to continue paying for fire hydrant services within Respondents' jurisdictions (CP 626-28), and that the hold harmless provisions preclude Tacoma's demand for payment and this lawsuit (CP 528-31).

Tacoma moved for partial summary judgment, claiming that the hold harmless obligations would only be triggered upon the filing of third party tort claims, and requesting a ruling that its cost calculation methodology is appropriate. CP 482-500. Pursuant to CR 56(f), the Respondents moved for additional time to respond to Tacoma's motion. CP 569-571. The Respondents pointed out that Tacoma had not yet answered the Respondents' discovery requests concerning TPU's

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[4] Tacoma claims that the utility has been absorbing the cost of fire hydrants in Respondents' jurisdictions, rather than recouping the cost from ratepayers. CP 480.

[5] The City of Bonney Lake and King County were named as defendants, but settled with Tacoma because of the small number of hydrants in each jurisdiction. CP 95-96, 520-21.

methodologies for calculating PFP costs. *Id.* In addition, the cities highlighted the fundamental unfairness of forcing municipalities to pay Tacoma for infrastructure that was installed years, even decades, before the cities incorporated. CP 626-27.[6]

In May 2010, Judge Douglass North denied Tacoma's motion and granted the Respondents', ordering, "The indemnification provisions of the above-referenced individual franchise agreements preclude the City of Tacoma from advancing this action against Defendants City of Fircrest, City of University Place, City of Federal Way, and Pierce County." CP 730. The court also ordered that Tacoma pay Federal Way's defense costs. *Id.* The trial court did not address Tacoma's request for declaratory ruling on its cost calculation methods, finding the indemnity provisions to be dispositive of all claims. CP 731. Tacoma moved for reconsideration, which the trial court granted in part (CP 728-31), and then sought direct review in this Court.

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[6] University Place, Fircrest, and Federal Way incorporated as cities organized under the Optional Municipal Code, Title 35A RCW, in 1995, 1990, and 1990 respectively. In addition to the impropriety of forcing a city to pay for infrastructure that was already in the right-of-way when the city incorporated, it is unfair to include in PFP costs an increment for "oversizing." Water mains are typically installed, and oversized, by private developers, and so Tacoma did not bear this cost. *See infra* Part III.G of this Brief.

III. ARGUMENT

A. This Court can affirm the trial court's summary judgment order on any appropriate grounds.

On appeal from a summary judgment order, the appellate court engages in the same inquiry as the trial court. *Okeson*, 150 Wn.2d at 549, citing *Key Tronic Corp. v. Aetna (CIGNA) Fire Underwriters Ins. Co.*, 124 Wn.2d 618, 623-24, 881 P.2d 201 (1994). Contract construction—that is, the process of determining the legal effect and ramifications of a contract—presents a question of law that the court reviews *de novo*. *Keystone Masonry, Inc. v. Garco Const. Inc.*, 135 Wn. App. 927, 932, 147 P.3d 610 (2006); *Berg v. Hudesman*, 115 Wn.2d 657, 663, 801 P.2d 222 (1990).

Judge North dismissed Tacoma's lawsuit because of the broad hold harmless provisions within the franchises. This Court should affirm the trial court's decision on this ground, or on the alternative ground that TPU has an ongoing contractual obligation to provide fire hydrant services pursuant to the franchises. *State v. Costich*, 152 Wn.2d 463, 477, 98 P.3d 796 (2004) (court can affirm summary judgment order on any grounds supported by the record).

This Court should confine its review to contract law, rather than addressing Tacoma's constitutional "tax vs. fee" arguments. *Citizens Alliance for Property Rights v. Sims*, 145 Wn. App. 649, 656, 187 P.3d 786 (2008)

(appellate courts should refrain from addressing constitutional issues where alternative grounds exist). To reach a decision in this case, this Court need not engage in an ethereal debate over taxation; it need only decline to interfere in the fair and legal contractual relationship forged between Tacoma and the Respondents.

B. Municipalities have the authority to contract, and their proprietary decisions are entitled to deference from the courts.

Tacoma has statutory authority to operate a water system, within and without its corporate limits. RCW 35.92.010. Operating a utility—a task made more efficient and cost-effective by franchise agreements with neighboring jurisdictions—is a proprietary function. *Burns*, 161 Wn.2d at 145-46, 155-56; *Okeson*, 150 Wn.2d at 547, 550. ("The principal test in distinguishing governmental functions from proprietary functions is whether the act performed is for the common good of all, or whether it is for the special benefit or profit of the corporate entity."). A municipal utility's proprietary decisions are entitled to deference from the courts. *Taxpayers of Tacoma v. City of Tacoma*, 108 Wn.2d 679, 694, 743 P.2d 793 (1987) ("[W]here the legislature authorizes a municipality to engage in a business, it may exercise its business powers in very much the same way as a private individual."); *Hite v. Pub. Util. Dist. No. 2*, 112 Wn.2d 456, 460, 772 P.2d 481 (1989) (when contracting in its proprietary capacity, a city "has a

right to insert in the contract any condition or conditions (not in themselves unlawful) which might be deemed beneficial or advantageous to its citizens").

TPU had full authority to enter into contracts with the Respondents in order to set the terms under which TPU would operate in each jurisdiction. *Burns*, 161 Wn.2d at 154-55. A municipality is under no obligation to supply utilities outside its corporate limits but if it elects to do so, the relationship forged with the receiving jurisdiction is purely contractual. *People for Preservation & Dev. of Five Mile Prairie v. City of Spokane*, 51 Wn. App. 816, 821, 755 P.2d 836 (1988), citing *City of Colorado Springs v. Kitty Hawk Dev. Co.*, 392 P.2d 467, 471 (Colo. 1964). A city may enter into any contract so long as it does not conflict with the constitution, a statute, or a city's own charter or ordinances. *Burns*, 161 Wn.2d at 155 (citation omitted).

Municipalities often elect to enter into franchises to set the terms for extra-territorial water service. *Burns*, 161 Wn.2d at 143 ("A franchise is the right of a public utility to make use of the city streets for the purpose of carrying on the business in which it is generally engaged, that is, of furnishing service to members of the public generally.") (citations omitted);

see also RCW 35A.47.040; RCW 36.55.010 (giving cities and counties statutory authority to grant franchises for utility services, including water).

This Court is required to construe the franchises in a manner that would preserve the contractual arrangement between the parties. *Eurick v. Pemco Ins. Co.*, 108 Wn.2d 338, 340-41, 738 P.2d 251 (1987) (goal of contract construction is to give effect to the agreement, with practical and reasonable results). This is especially true with a mutually-beneficial franchise negotiated between municipalities, which have the full freedom to contract. *Burns*, 161 Wn.2d at 155-56. The broad authority municipalities have to negotiate contracts mandates a "hands off" approach from the courts.

C. The franchises cannot be construed to require the payment of money for fire hydrants.

TPU's franchises with the Respondents contain clear language authorizing Tacoma to construct, maintain, and repair its water system. CP 191, 225. Nowhere do the franchises exclude components attributable to fire suppression from the "water system;" in fact, it would make no sense to exclude them. State law defines "water system" to include fixtures and appliances used in connection with the supply of water for municipal purposes. RCW 80.04.010. Fire hydrants are no doubt "appurtenances" or "appliances." The franchise agreements indicate that TPU would maintain

the water system, and in turn the Respondents would allow it to exist within their jurisdictions. Tacoma's right to "maintain" the water system must be construed as a corresponding obligation to take full responsibility, and pay, for it. As Judge Spearman correctly ruled in *Lane*, in executing a franchise with the Respondents, Tacoma agreed to bear the costs of the system, and waived any claims for reimbursement. CP 420.

None of the franchises require the Respondents to pay TPU cash for fire hydrant services. To impose such an obligation now would be to insert a term into the franchises that the parties did not choose to adopt. Courts cannot impose obligations between parties that never existed, nor can they expunge lawful provisions agreed to and negotiated by the parties. David K. DeWolf et al., *25 Contract Law and Practice* § 5:4 (2d ed. 2007). The courts are not permitted to create a contract for the parties which they did not make for themselves. *Id.* (citing *Seattle Prof'l Eng'g Employees Ass'n v. Boeing Co.*, 139 Wn.2d 824, 991 P.2d 1120 (2000)). Courts may not substitute their judgment for that of the parties to rewrite the contract or interfere with the internal affairs of corporate management. *Clements v. Olsen*, 46 Wn.2d 445, 448, 282 P.2d 266 (1955).

Moreover, TPU's course of conduct shows that prior to *Lane*, it fully intended to provide fire suppression services for the life of the franchises.

Puget Sound Fin., LLC v. Unisearch, Inc., 146 Wn.2d 428, 47 P.3d 940 (2002) (course of conduct is a pertinent factor in construing a contract). Since the time the franchises were executed, to 2008 when Tacoma decided to bill the Respondents, Tacoma has provided fire hydrant services in Respondents' jurisdictions without asking for payment. Even after *Okeson* in 2003, when Seattle saw the writing on the wall and stopped billing ratepayers for fire hydrants, Tacoma did not ask for payment. This Court should not now override the terms of the franchises and a decades-long course of conduct pursuant to those terms. After these franchises expire, the parties are free to re-negotiate.

Tacoma points out that when the franchise agreements were executed, *Lane* had not yet been decided. Brief at 4. But Tacoma simultaneously argues that *Lane* did not change the law. Brief at 25 n. 3 ("*Lane* did not reverse a statute or create new law; this Court simply enunciated how existing law should be applied in water rate making practices."). Before and after *Lane*, Tacoma had the ability to negotiate a franchise with Respondents that required the Respondents' general funds to pay for fire hydrants. Tacoma never did so. Instead, it now attempts to use a judicial decision which, by its own admission, "did not create new law," to override its contractual obligations. This Court should not re-write

the agreement of the parties, when doing so would fleece the Respondents and hand Tacoma a windfall.

D. The franchises establish a contractual relationship, with consideration flowing to both sides.

A universal quality of franchises is that they are mutually beneficial. *City of Lakewood v. Pierce County*, 106 Wn. App. 63, 74, 23 P.3d 1 (2001). As this Court held in *Burns*:

> The grant of a franchise is a special privilege that allows particular individuals to profit from the use of the city streets in a manner not generally available to the public as a common right.

Burns, 161 Wn.2d at 143 (citation omitted). Utilities are susceptible to economic incentives, including the motivation to maximize gains and minimize losses; therefore, a utility will not enter into a franchise unless it is financially prudent. *Taxpayers of Tacoma*, 108 Wn.2d at 690 (municipal utility "has disincentives to investing its own money in measures that are not cost effective"), cited in *Burns*, 161 Wn.2d at 148. Because a municipal utility naturally seeks to minimize costs and maximize efficiency, the franchises must be presumed to be cost-effective for TPU. *Taxpayers of Tacoma*, 108 Wn.2d at 690. Precise mathematical quantification of the benefit TPU receives from the franchises is not required; only a practical basis must be shown. *Teter v. Clark County*, 104 Wn.2d 227, 234, 704 P.2d

1171 (1985); *King County v. Taxpayers of King County*, 133 Wn.2d 584, 597-98, 949 P.2d 1260 (1997).

Another universal quality of utility franchises is that they are voluntary. A municipality cannot require a utility to enter into a franchise, nor can it force the utility to accept the terms of a franchise. *City of Lakewood*, 106 Wn. App. 63; *Burns*, 161 Wn.2d at 142. However, a municipality may entirely refuse to grant a franchise. *City of Spokane v. Spokane Gas & Fuel Co.*, 175 Wn. 103, 107, 26 P.2d 1034 (1933), cited in *Burns*, 161 Wn.2d at 143. Refusal to grant a franchise leaves a utility operating in the streets of another municipality without a contract that guarantees it the continued right to be there. For a utility with infrastructure as sprawling and expensive as TPU's, this can be a perilous position to occupy.

The desire to avoid that peril is exactly why the franchises constitute valuable consideration to Tacoma, despite its current protests to the contrary. CP 5. There could be no dispute that TPU needs to maintain its rate base and economy of scale in order to provide efficient and cost-effective service to its customers. *Burns*, 161 Wn.2d at 156. As this Court noted in *Lane*, the cooperation of neighboring municipalities is crucial to TPU's ability to operate an efficient water utility. *Lane*, 164 Wn.2d at 890

("SPU will not likely install fire hydrants where uninvited. Right-of-way problems alone would block this eventuality."). The franchises grant TPU an affirmative right to occupy the rights-of-way. As long as the franchises remain in effect, TPU will not need to condemn easements via an exercise of eminent domain—an expensive proposition for the utility. Nor will it face undue opposition in getting permits for maintenance and expansion. Nor should it face threats that municipalities would condemn TPU's infrastructure through an exercise of eminent domain. Perhaps most importantly, TPU can keep the ratepayers in Respondents' jurisdictions on its books. All of these certainties together are of value to TPU; otherwise, it would not have bothered executing franchises with the Respondents in the first place.

A franchise is such a valuable privilege that utilities often agree to pay franchise fees as "rent" for the utility's use of the streets. *City of Spokane*, 175 Wn. at 108. As this Court recognized in *Burns*, municipalities may elect to receive payment in the form of "free services" rather than cash:

> Because a franchise is a valuable property right, it is a privilege for which cities, historically, have exacted compensation in the form of free services or a cash payment.

Burns, 161 Wn.2d at 144, citing *State ex rel. Pac. Tel. & Tel. Co. v.* , 19 Wn.2d 200, 278, 142 P.2d 498 (1943).[7] The franchises established a balanced contractual relationship through which certainty flowed to TPU, and fire suppression services flowed back to the Respondents. This Court should not now unbalance the deal by forcing the Respondents to pay Tacoma for a service it agreed to provide.

E. The hold harmless provisions preclude Tacoma's claims for any costs arising from the franchises, including fire hydrants.

The hold harmless provisions contained within the franchises are broad enough to preclude Tacoma's lawsuit against the Respondents. Such broad indemnity clauses are allowed by law. *See MacLean Townhomes, LLC v. America 1st Roofing & Builders, Inc.*, 133 Wn. App. 828, 832-33, 138 P.3d 155 (2006). Hold harmless clauses are subject to the fundamental rules of contract interpretation, which require "reasonable construction so as to carry out, rather than defeat, the purpose." *Cont'l. Cas. Co. v. Municipality of Metro. Seattle*, 66 Wn.2d 831, 835, 405 P.2d 581 (1965).

[7] Neither Federal Way nor Pierce County charges TPU any fees at all. University Place and Fircrest do charge a fee, but have agreed not to compete with TPU. CP 216-17, 196. A "non-compete fee" is bargained for by a municipality acting in its proprietary, not governmental, capacity, and is therefore not regarded as compensation for a franchise. *Burns*, 161 Wn.2d at 151 (Seattle City Light's payments to municipalities in exchange for non-compete clause were "incurred in the context of a proprietary transaction," and therefore outside the franchise).

The obligation to "hold harmless" operates as a waiver of any claims Tacoma might have otherwise had against the Respondents. The broad language of the hold harmless provisions demonstrates the parties' intent that the Respondents incur no costs as a result of the franchises. Similarly, language obligating Tacoma to "release" or "covenant not to sue" precludes this lawsuit against the Respondents. CP 195, 212. The *Restatement of Contracts* defines a "release" as "a writing providing that a duty owed to the maker of the release is discharged immediately or on the occurrence of a condition." *Restatement (Second) of Contracts*, §§ 284-85 (1981). A covenant not to sue is defined as "a contract under which the obligee of a duty promises never to sue the obligor or a third person to enforce the duty or not to do so for a limited time." *Id.*; *Boyce v. West*, 71 Wn. App 657, 662, 862 P.2d 592, 595 (1993) (noting that releases are construed according to contract principles). Thus, both a release and a covenant not to sue relinquish a right that Tacoma possesses or will possess, and do not involve the rights of any third party. In addition, neither a release nor covenant not to sue is necessarily limited to tort actions.

Tacoma asserts, without any legal authority, that the hold harmless provisions only protect the Respondents from tort claims. But on its face, the contractual language is not so limited. Rather, the franchises require

TPU to defend, indemnify, hold harmless, and in some cases release and covenant not to sue, from "any and all claims." CP 195 (Fircrest), 212 (University Place), 235 (Federal Way), 253 (Pierce County). Use of the phrase "any and all" extends the obligation beyond tort claims. *Cambridge Townhomes LLC v. Pacific Star Roofing, Inc.*, 166 Wn.2d 475, 487, 209 P.3d 893 (2009); *Maclean Townhomes*, 133 Wn. App. at 832-33.

If Tacoma had intended to limit its obligations to tort liability, it could have expressly stated so. But the franchise agreements indicate the opposite intent; all four of them enumerate "liability" as only one circumstance that may trigger the obligation to defend, indemnify, and hold harmless. *See, e.g.*, CP 253 (". . . from and against all liability, loss, cost, damage, and expense."). The language expressly covers all costs "arising out of" the franchise. CP 195, 212-13, 235 (" . . . arising from, resulting from, or connected with this Franchise . . . "), 253. There could be no dispute that fire hydrant costs "arise out of" TPU's presence in the Respondents' jurisdictions, which is the very subject matter of the franchises. But for TPU's water mains, there would be no TPU fire hydrants.

Tacoma erroneously argues that its obligation to hold the Respondents harmless is not triggered absent a third party lawsuit. The language does not limit its coverage only to third parties. Rather, the

defense, indemnity, and hold harmless obligations extend to "any person or entity." *Id.* Tacoma could have added the words "filed by third parties" after the word "claims," but did not do so. Moreover, there could easily be a third party involved here: the ratepayers. Tacoma chose to bill the Respondents for hydrants before a *Lane*-style ratepayer lawsuit was filed. But if such a lawsuit were filed and resulted in litigation costs being imposed on the Respondents, there would be no doubt that TPU would have to hold them harmless from these costs. The hold harmless provisions are no less operable in the absence of a ratepayer lawsuit.

F. Enforcing the franchises would not violate public policy.

As noted, this Court should avoid engaging in the thorny debate over the constitutional parameters of taxation. Addressing this issue is wholly unnecessary to the result, when the Court need simply hold the parties to their contractual obligations. Nevertheless, it is clear that the franchises, if interpreted to preclude cash payments in exchange for fire suppression services, do not violate the constitution; nor are they "void against public policy."

A contract is only void against public policy when it is condemned by judicial decision, prohibited by statute, or contrary to the public morals. *Brown v. Snohomish County Physicians Corp.*, 120 Wn.2d 747, 753, 845 P.2d

334 (1993). No party contends that the franchises are "contrary to the public morals." Rather, Tacoma argues that the franchises, if construed so as to require it to continue to provide hydrant services to the Respondents, are condemned by judicial decision (*Lane*) and prohibited by statute (RCW 43.09.210). Neither is the case.

Tacoma repeatedly accuses the Respondents of trying to foist their general government responsibility onto "Tacoma ratepayers," thereby imposing an "illegal tax." *E.g.*, Brief at 6. Such arguments are misleading on many levels. First, the issue of whether Tacoma would choose to increase rates to pay for extra-territorial fire hydrants, if the Respondents do not pay, is not before the Court; unless or until TPU adds fire hydrants costs back into rates, the "tax vs. fee" debate is merely academic. Second, if TPU did choose to raise rates, the Respondents would not be "taxing" anyone; they would merely be enjoying the consideration given in return for the franchises. Third, Tacoma's argument that the cost would impermissibly fall on "Tacoma ratepayers"—suggesting only ratepayers who reside in Tacoma (Brief at 4)—is disingenuous. TPU might choose to charge all ratepayers, including those in Federal Way, Fircrest, University Place,

and Pierce County, as a cost of doing business. In fact, that is exactly what TPU was doing prior to *Lane*.[8]

Pursuant to *Lane* and other precedent, TPU has the authority to agree to provide fire hydrant services, and to hold the Respondents harmless from costs, as consideration for operating its utility in Respondents' jurisdictions. It also has the authority to incur, and recoup, business expenses resulting from its utility operations. *Lane* requires only that Tacoma follow constitutional requirements regarding the enactment of taxes, if in fact a tax is being imposed. *Lane*, 164 Wn.2d at 886. No "tax" is being imposed in this case.

In *Covell v. City of Seattle*, 127 Wn.2d 874, 879, 905 P.2d 324 (1995), this Court articulated a three-part test for determining whether a charge is a tax or a fee. The Court looks to the purpose of the cost, where the money raised is spent, and whether people pay the cost because they use the service. *Id.* While a municipality must be authorized by statute to

[8] Tacoma asserts the "sky is falling" prediction that, if this Court sustains the trial court's ruling, TPU will be forced to "discontinue its maintenance of the Defendants' fire hydrants for local fire services, and it will no longer be able to provide oversized infrastructure to entities that cannot ensure payment." CP 481. Such predictions have no merit. There is an easy solution to TPU's dilemma: recoup its business costs from its broad ratepayer base. RCW 35.92.010 allows a utility to set different rates for different utility customers, depending on the cost of service. Tacoma could use this flexibility to design a rate structure that accounts for the cost of delivering services in different jurisdictions.

impose a tax, a municipal utility has broader authority to impose a fee. *Lane*, 164 Wn.2d at 882. As the *Okeson* Court noted, a utility fee does not become an unlawful tax simply because it "raises revenue":

> It is a misnomer to simply ask whether the charges raise revenue, because both taxes and regulatory fees raise revenue. What is important is the purpose behind the money raised—a tax raises revenue for the general public welfare, while a regulatory fee raises money to pay for or regulate the service that those who pay will enjoy (or to pay for or regulate the burden those who pay have created).

Okeson, 150 Wn.2d at 552-53. Applying the *Covell* factors, the *Okeson* and *Lane* Courts found that charges for street lights and fire hydrants, in general, constitute taxes and not fees. *Okeson*, 150 Wn.2d at 553-54; *Lane*, 164 Wn.2d at 882-83. However, neither of those cases dealt with the issue of whether a utility can charge ratepayers for costs incurred under a mutually-beneficial franchise.

If fire suppression services are provided pursuant to a franchise, the purpose of increasing water rates to cover the cost would not be to raise revenue for Tacoma's general government, but to compensate TPU for honoring its contractual obligations. Such a rate increase would help pay for the commodity enjoyed by TPU ratepayers—low cost and efficient water service facilitated by the franchises. *See* Hugh Spitzer, *Taxes vs. Fees: A Curious Confusion*, 38 Gonz. L. Rev. 335, 344-45 (2003) (utilities may

impose "commodities charges" that are reasonably proportionate to the customer's allocable share of the capital and operating costs of providing the commodity or service). Thus, the increased water rate would merit the label of "fee"—or, more correctly, "commodity charge"—and not "tax." *Lane* does not foreclose this result.

Similarly, the State Accountancy Act, RCW 43.09.210, does not preclude an arrangement by which TPU provides fire hydrant services to Respondents' jurisdictions, and agrees to hold the jurisdictions harmless for the costs of same, in exchange for a franchise. The Respondents do not suggest that Tacoma could pay for fire hydrants in their jurisdictions out of its general fund. Such an arrangement would violate RCW 43.09.210. *Lane*, 164 Wn.2d at 889, n. 2 (precluding "resident taxpayers of the providing city [from] paying for services to others"). But TPU, unlike Tacoma's general fund, made a business decision to enter into franchises with the Respondents, in light of the benefits conveyed. Such an arrangement does not violate RCW 43.09.210 because TPU receives value for the service it provides. Tacoma taxpayers would not be footing the bill for a service in another jurisdiction; TPU ratepayers would be paying for low cost, efficient utility service made possible through the franchises.

The Accountancy Act does require that municipalities exchange property or services for "true and full value." However, the standard for determining "true and full value" is deferential. The courts have repeatedly declined to require "mathematically certainty" in a utility's financial decisions, or to second-guess the adequacy of consideration provided for a government benefit, as long as a reasonable basis for the exchange can be shown. *Teter*, 104 Wn.2d at 234; *Taxpayers of King County*, 133 Wn.2d at 597-98.

Finally, Tacoma's suggestion that the franchises are a "dry hole," such as that which was declared invalid in *Chem. Bank v. Wash. Pub. Power Supply Sys.*, 99 Wn.2d 722, 66 P.2d 329 (1983), is misplaced. This Court declared the WPPSS bond financing scheme to be an illegal "dry hole" because it "committed ratepayers to an enormous financial risk, irrespective of whether the [nuclear power] plants ever produced electricity." *Taxpayers of Tacoma*, 108 Wn.2d at 700. Such concerns are not implicated here because TPU's entire rate base benefits from an economy of scale the franchises help provide. *Burns*, 161 Wn.2d at 156. The franchises here are not a "dry hole;" they are balanced business deals that should be left intact.

G. The Court should not reach any decisions on TPU's proposed method of calculating PFP costs.

Tacoma asks this Court to declare that its methodology for calculating hydrant costs is appropriate; in fact, it asserts that the Court is required to do so pursuant to the Declaratory Judgments Act, Chapter 7.24 RCW. TPU appears particularly interested in obtaining a ruling that the costs attributable to "oversizing" the water mains can be included in PFP cost calculations.

The Respondents do not dispute that, to be operational, a fire hydrant must be connected to a water main that can provide adequate fire flow. However, Respondents vigorously dispute what costs are attributable to which components of the water system. Respondents have never conceded that Tacoma's method for calculating PFP is appropriate. In fact, the Respondents question whether Tacoma properly accounted for "oversizing." At the trial court level, the Respondents objected to the fundamental unfairness of requiring the cities to pay for oversized infrastructure that was already in the ground when the cities incorporated. CP 626-27. The Respondents also question whether Tacoma has properly discounted PFP costs to reflect the fact that TPU did not pay to install most of the infrastructure. State law authorizes the common practice of requiring private developers to extend the water system, with

reimbursement possible through a latecomer agreement. RCW 35.91.020. Tacoma provided no information to confirm it had properly accounted for infrastructure costs. *See* CP 86.

Tacoma's contention that this Court is *required* to declare the rights of the parties in a declaratory judgment action (Brief at 28) is inaccurate. In *Greyhound Corp. v. Division 1384*, 44 Wn.2d 808, 271 P.2d 689 (1954), this Court indicated that the trial court should have declared that the appellant did not have the rights it sought pursuant to the contract, rather than dismissing the action for "failure to state a claim." But Judge North did not dismiss Tacoma's lawsuit for "failure to state a claim." He dismissed it because the indemnity provisions of the franchises do not give Tacoma a right to sue the Respondents for fire hydrant costs. Nothing in *Greyhound* obligates the Supreme Court—on appeal from a dismissal by the trial court—to declare rights that are not material to the result.

In addition, this Court lacks an adequate record upon which to determine the propriety of Tacoma's cost calculations. The trial court also lacked such a record; largely due to Tacoma's failure to answer the Respondents' discovery requests prior to moving for summary judgment. This Court is not required to reach an issue for which an inadequate record exists:

> [T]here are many reasons arguments raised in the briefs may not be addressed in the opinion. The factual predicate may not appear in the record; the argument may not have been raised appropriately below; the issue may not have been properly raised in the petition or the answer; the court may simply feel it unnecessary to address them to reach a just adjudication. An appellate court is not a performing bear, required to dance to each and every tune played on an appeal.

Lummi Indian Nation v. State, No. 81809-6, (Wash., Oct. 28, 2010) n.1 (citation and internal quotations omitted). Even if this Court were to find that the issue of Tacoma's cost calculations should be addressed, at most it should remand to the trial court to make a full and accurate record.

H. Tacoma's motion for fees under RAP 18.1 is without merit; Tacoma has a duty to defend Federal Way.

It is well-settled law that the duty to defend is broader than the duty to indemnify. *See, e.g., American Best Food Inc. v. Alea London, Ltd.*, No. 80753-1 (Wash., Mar. 10, 2010). A complaint must be liberally construed to see if there is any possibility that the party owed the defense could incur financial liability. *Id.* If so, the duty to defend has been triggered, even if a court ultimately finds no duty to indemnify. *Id.* Tacoma filed this lawsuit after Judge Spearman had already ruled, in the *Lane* case, that franchise agreements containing broad indemnity provisions sheltered King County and Shoreline from SPU's claims. There was every reason for Judge North, and Tacoma, to believe that the Respondents were similarly entitled to be

held harmless from TPU's claims. This most certainly triggered Tacoma's duty to defend Federal Way.

Tacoma's request for fees under RAP 18.1 is misplaced. Tacoma is paying Federal Way's attorney fees because the trial court determined it had a duty to defend. Nothing in RAP 18.1 suggests that an award of defense costs, pursuant to an indemnity provision, should be reversed if a court finds no duty to defend. If Tacoma did not want to incur liability for defense costs, then it should have honored its contractual arrangement with Federal Way, rather than suing the Respondents for costs it can, and must, lawfully bear.

IV. CONCLUSION

Aware of the benefits franchises would offer, including the ability to keep its enormous rate base and sprawling infrastructure intact, Tacoma entered into voluntary contractual relationships with all the Respondents. The franchises do not obligate the Respondents to pay Tacoma money to cover the costs of fire suppression services. Until the end of 2008, when Tacoma decided to surprise the Respondents with very large bills, TPU covered the cost of this service and billed it to its ratepayers as part of the cost of operating the water system as a whole. Prior to *Lane*, the parties understood this to be a fair deal. Nothing in *Lane* renders the arrangement

unfair or illegal. The parties, especially when acting in their proprietary capacities, have the power to contract. Along with this power comes the freedom to craft terms they regard as beneficial. In fact, as a utility provider, TPU is presumed to act in its economic self-interest. TPU also has the power to recover business expenses, including consideration given in exchange for a franchise, from its ratepayers.

Tacoma asks this Court to interfere in the parties' long-standing relationships and add a contract term that the parties did not negotiate for themselves. This Court should decline that invitation. Tacoma agreed to provide fire hydrants; it agreed not to sue; it agreed to defend, indemnify, and hold harmless. This Court should not excuse Tacoma from those obligations now. For all these reasons, the Respondents respectfully request that the Supreme Court uphold the trial court's grant of summary judgment in favor of the Respondents.

RESPECTFULLY SUBMITTED this 17th day of December, 2010.

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